APPLE TAX –The Core Issues.

© Professor Dr. Irene Lynch Fannon, School of Law, University College Cork, IRELAND. May 2017.

This is a draft paper. Please note that comments are very welcome but you are requested not to use this material without permission or citation.

Introduction

The corporation is one of a number of market actors which create value but at the same time can and ought to behave in ways which are economically sustainable. In the context of this paper this means that corporate actions ought to satisfy the economic needs necessary for stable and resilient societies. There is a clear imperative that multinational companies are not governed by an agenda dominated by a notional concept of 'shareholder primacy' which will lead to many unsustainable behaviours including the aggressive avoidance of tax liabilities. Whilst the problems associated with the concept of 'shareholder primacy' have been well documented, it is entirely plausible that there are other dynamics at play in relation to understanding corporate actions. This paper will address this hypothesis regarding additional motivations when it considers corporate culture. Aggressive avoidance of tax liabilities on the part of multinational corporations has been the focus of considerable work by the OECD reflected in its Report on Base Erosion and Profit Shifting Project (Final Report) 2015. [1]

Ireland, along with 23 other sovereign states is a signatory to the BEPS agreement. Yet since the mid 1980s Ireland has pursued a low corporate tax rate as part of a national strategy to attract foreign direct investment into Ireland. The corporate- friendly low tax rate of 12.5 % enjoys populist support as a 'job creation' strategy, despite high personal income tax rates ranging from 20%- 45% approximately. This may seem strange in other more complex societies but this strategy is universally supported in Ireland and hardly ever questioned, even by those who are politically on the left. In August 2016 the EU Commission ruled that a globally respected 'corporate citizen'-Apple Inc.-had underpaid taxes arising from sales in Europe by a sum of 13billion Euros and that Ireland, a small member of the European Union, was responsible for collecting this tax. Ireland is appealing this decision. (Other large multinational companies such as Google, Facebook and large pharmaceuticals have presences in Ireland).

Avoidance (distinguished here from illegal evasion) of tax on the scale we are considering is destructive and antithetical to sustainable actions. 13 billion Euros represents a significant sum of monies required by governments to fund schools, hospitals, infrastructure and even aid programs (states fund their development aid programmes to global regions through taxation). This paper places the interplay between Apple Inc., the Irish and US national tax authorities (California and US Federal), the EU Commission and OECD global tax initiatives such as BEPS (Base Erosion Profit Shifting) within two theoretical frameworks. It will consider the interplay of national, international and supranational regulatory systems, within the concepts of 'regulatory ecology' and multi-level regulation[2] with

[1] See generally www. oecd.org and in particular regarding the OECD BEPS Final Report 2015. http://www.oecd.org/ctp/beps-explanatory-statement-2015.pdf

[2] My thanks to my colleagues and collaborators in the SMART project based at the University of Oslo Faculty of Law for their insights into these two theoretical frameworks. I am grateful in particular to Karin Buhman of the

particular focus on the relationship between legal and social norms (the acceptability of tax avoidance). My hypothesis is that this particular case study presents a ‘perfect storm’ allowing us to see how these regulatory arenas and types interface rather badly with each other. This is not a simple story of corrupt corporate or bureaucratic actions but rather a presentation of a complex range of problems which cannot be addressed by rushing to ill-considered conclusions. The problems include the interests of multinational regulatory organisations (the OECD), of sovereign states, in particular the United States, California and Ireland, the interests of the EU Commission as a federal regulatory authority including its relationship to Ireland as a member state, and finally the interests of a large multinational corporation, namely Apple Inc.

Context

In August 2016 the European Commission issued a decision that Ireland had given ‘illegal state aid to Apple Inc.’ to the tune of €13 billion. In a press release dated 30 August 2016, entitled **State aid: Ireland gave illegal tax benefits to Apple worth up to €13 billion** which summarised this decision for the public, the European Commission stated that it had

> “concluded that Ireland granted undue tax benefits of up to €13 billion to Apple. This is illegal under EU state aid rules, because it allowed Apple to pay substantially less tax than other businesses. Ireland must now recover the illegal aid.”

The Commission stated that this decision on the part of the Irish state which amounted to selective treatment allowed Apple Inc. “to pay an effective corporate tax rate of 1 per cent on its European profits in 2003 down to 0.005 per cent in 2014."

This ruling has been the subject of considerable media commentary since that time. Almost immediately the focus in Ireland was on the role of the Irish Government. Concerns were expressed about the nature of the decision making within one of the hitherto most respected state regulators, the Revenue Authorities. In addition a great deal of public and media concern focused on Ireland’s relationship with the EU and the extent to which that relationship would be damaged by this decision. A further source of concern was the damage this decision would do to Ireland as a location for multinational corporate investment, which is generally considered to be quite a significant driver of Ireland’s economic wellbeing.[3] Interestingly very

Copenhagen Business School for her insights into multi level regulation as a variant of multi level governance theories. This paper was first delivered at a conference on Trade and Investment, Oslo Faculty of Law, May 2017. http://www.smart.uio.no/
I am also grateful to my colleague Declan Walsh, School of Law, University College Cork for his insights into the competition law aspects of the Commission’s ruling.

[3] Nolan, Brian, O’Connell, Phillip J and Whelan, Christopher,: Conclusion: The Irish experience of Growth and Inequality in BUST TO BOOM? (NOLAN, BRIAN, O’CONNELL, PHILLIP J AND WHELAN, CHRISTOPHER EDS. 2000) and KENNEDY K.A., GIBLIN, T. AND MCHUGH, D: THE ECONOMIC DEVELOPMENT OF IRELAND IN THE TWENTIETH CENTURY. (1989)
LEE, J. J: IRELAND: 1912-1985: POLITICS AND SOCIETY (CAMBRIDGE UNIVERSITY PRESS, 1989)
See further Economic and Social Research Institute (Ireland) www.esri.ie.
Enterprise Ireland www.enterprise-ireland.com
The Industrial Development Authority. (Ireland) www.idaireland.com

little attention was paid to the position of Apple Inc. and its apparent culpability in the avoidance of its tax obligations. This culpability is not of a legal nature strictly speaking, unless the Commission's ruling remains intact, but even without a ruling of illegality, there are clear ethical issues concerning aggressive tax avoidance on this scale.

As it happens Apple Inc's. operational activities in Ireland are based primarily in a plant in Cork and so one of the reporters from the national radio station based in Cork secured an interview with Tim Cook the CEO of Apple. In a later part of this paper I will consider some aspects of this interview and address the role of the corporation in relation to the problem of tax avoidance. This paper will consider this issue from a number of perspectives, the first is the overall issue regarding the appropriate taxation of corporations so that corporations contribute in a fair and balanced manner to the communities and social infrastructure in which they are embedded. In my paper these concepts are broadly understood. Second the paper will consider the position of the Irish and US governments. Third the paper will consider the role of the EU Commission. Finally, the paper will conclude on a consideration of corporate culture and why avoiding the payment of tax is a problem which like many must be addressed from the broader perspective of sustainable corporate and business models.

Tax Avoidance- A Global Issue.

Corporate tax avoidance, which is legal and to be distinguished from tax evasion which is illegal, is a global problem which should be of interest to the average person on the street because it is an issue of equality and social justice. Multinational companies (MNCs) take advantage of different tax codes to reduce their tax burden. Tax avoidance by multi-nationals is very easy to achieve for a number of reasons, the legal concept of corporate personality which allows for corporate groups to separate their activities into different corporate entities, corporate mobility, the ability to ruthlessly avail of low tax, low regulation jurisdictions[4] and finally, a lack of cohesion between different jurisdictional rules and a lack of knowledge on the part of other countries of different tax systems.

The success of the FDI strategy led to the following statement from two of the state agencies mentioned here regarding the position of Ireland in the mid 1990s onward. However the position has changed again with the current decade seeing considerable outward investment from Ireland also. See CSO figures 2016 *infra n. 9.* "The presence of a substantial foreign owned industry sector generates a substantial repatriation abroad of profits and dividends, which must be deducted in the calculation of GNP. As a consequence, on average, Ireland's GDP measure exceeds GNP by a factor of between 20-25%, which is a crude measure of the overstatement of income, or living standards for Ireland, that is inherent in use of the international standard GDP measure." Enterprise Ireland: Ireland; Economic Profile www.enterpriseireland.com
See further OECD ECONOMIC SURVEY: IRELAND (2006).

[4] Many scholars have noted the propensity of MNCs and TNCs to shop around jurisdictions. The reasons multinational corporations and transnational corporations create domestic overseas subsidiaries are varied but they are often in part driven by the availability of cheap labour, no or little taxes and in relation to the environment, no rules/ no enforcement. See further Kevin P. Gallagher and Lyuba Zarsky, The Enclave Economy. Foreign Investment and Sustainable Development in Mexico's Silicon Valley , The MIT Press (2007) ISBN 978-0-262-57242-2 214; Mabey, Nick and McNally, Richard: Foreign Direct Investment and the Environment- From Pollution Havens to Sustainable Development. OECD 1999..
As observed by Wright and Gray, 'the TNC is a 'forum shopper par excellence' Claire Bright-Staath and Benedict Wray: Corporations and Social Environmental Justice http://ssrn.com/abstract=2207317

The OECD launched its Base Erosion and Profit Shifting Project (BEPS-Final Report 2015)[5] and the EU launched its Anti-Tax Avoidance measures in January 2016 to address legal loopholes which are central to these activities. Ireland is a signatory to the OECD BEPS. The reduction of tax revenues otherwise payable to governments across the world, affects public funding for schools, hospitals, roads and social services. It also reduces the amount of funds available to developed countries to support aid activities in developing countries. Accordingly, there are ethical issues regarding these activities.

The OECD BEPS Final Report issued 15 primary recommendations to address this global shortfall in tax take. Of these the provisions addressed to what are called Hybrid Mis-Matches are central to the issues at stake in the Apple case. What was colloquially called the "Double Irish" [6] is an example of a variant of this mis -match issue.[7] This practise is no longer effective in Ireland as of January, 2015 (if already in use, abolished from 2020)

One of the other issues identified in the OECD BEPs Report is the broader problem where the legal structure does not reflect the substantial activity within the MNC group. The "Double Irish" and its variants is and was an example of this. The EU Commission ruling also focusses on this concept of economic reality as illustrated below. The following is an infographic issued by the European Commission at the same time as the publication of its decision regarding Apple Inc. in August 2016. It provides a clear illustration of the transfers involved. At the core of the problem is the agreement to attribute most or all of the profits from exploitation of IP through sales in Europe to 'head office' companies which are off-shore.

[5] See generally *OECD/G20 Base Erosion and Profit Shifting Project.* OECD Taxation Policy Group www.oecd.org and the statement of OECD Tax Authority on the fact that Ireland is not considered a 'tax haven' despite considerable criticism from the US.

[6] This involves the following steps:-

Intellectual property used outside the US is transferred by a US company to a company incorporated in a recognised tax haven (Co 1). Co 1 licenses the IP to Co 2 which is Irish incorporated and Irish resident Co 2 receives royalties for the use of the IP worldwide excluding the US. In particular in this case Co. 2 receives royalty payments relating to European sales. Co 2 then pays a royalty to Co 1. Co 2 gets a deduction for the royalty paid to Co 1 thus reducing its corporation tax bill. Co 1 is not subject to Irish tax as it is not resident in Ireland. Co 2 does not pay tax on the royalty from Co 2 sales as these are transferred to Co 1. In turn Co 1 is taxed in the tax haven alone at 0%

The Irish Government has restricted the use of the 'Double Irish' from 2015
It will be phased out by 2020.

[7] The section of the OECD BEPS Final Report 2015 on *Neutralising the Effects of Hybrid Mismatch Arrangements, Action 2 - 2015* is available HERE

Ireland Inc.

Ireland has adopted a low corporate tax rate of 12.5% as part of its strategy to attract foreign multinationals to Ireland. Originally this tax rate was set a 10% and only applied to foreign multinational manufacturing companies but now this tax rate is applied generally to Irish corporates.[8] As an element of a broader strategy to attract multinationals to Ireland this has proven to be extremely successful[9] and as of 2017 a large number of multinational companies,

[8] Taxes Consolidation Act, 1997 (Act No. 39/1997) (Ir.) http://www.irishstatutebook.ie/eli/isbc/1997_39.html (as amended-Latest Access 30/04/2017). These significantly lower than average tax rates on corporations are sustained somewhat controversially, both nationally and internationally with pressure from the European Commission on Ireland to raise rates to a more "European level". Accordingly, tax on manufacturing and other companies was originally 10% but was phased out in 2010. These are also somewhat controversial domestically when compared with the tax rates on individual income which is much higher at 42% (at the highest rate), although this is again lower than the European average of 45.3%. See further for some aspects of this planning Lynch Fannon, I: THE LUCK OF THE IRISH OR JUST PLAIN OLD TAX AND REGULATORY PLANNING? THE SUCCESS OF VENTURE CAPITALISM IN IRELAND.2006 Entrepreneurial Business Law Journal 1

[9]The Irish Central Statistics Office released up to date information in November 2016 indicating the position of Ireland regarding foreign direct investment. Interestingly in modern times Ireland's investment overseas is also an increasingly important factor. The CSO notes that "Irish stocks of direct investment abroad increased to €815bn at the end of 2015 from a stock position of €510bn at the end of 2014.This increase continues to be driven by the Redomiciled PLCs in Ireland…The rise between the end of 2014 and the end of 2015 was largely due to increased investment in enterprises located in Luxembourg (€240bn) and the US (€48bn). Further investment in Europe went to enterprises located in UK (€11bn), the Netherlands (€6bn) and offshore centres (€5bn) while Investment in Central American offshore centres decreased (€38bn)." Inward investment figures continue to grow also. "The stock of foreign direct investment into Ireland also increased between the end of 2014 and the end of 2015 - from €343bn to €796bn. The main contributors were increased investment from the US (€349bn), from Luxembourg (€69bn), the Netherlands (€11bn) and from all offshore centres (€38bn)". However the figures show that "The net

both from the US and Europe have based their activities in part in Ireland.[10] Even though this low corporate tax rate has been controversial in recent years in European quarters, the EU Commission made it quite clear that its current decision regarding Apple "does not call into question Ireland's general tax system or its corporate tax rate."
It is important to remember that the EU Commission does not have competence in relation to domestic taxation matters and so therefore the EU does not have authority to set the corporation tax rate or indeed any other tax rate for EU member states. In contrast the EU Commission does have competence in relation to competition matters and so this is one of the reasons that this matter has been dealt with by the DG of the EU dealing with Competition within the internal market, headed up by EU Commissioner for Competition (Anti-Trust) Margarethe Vestager, and that the problem has been couched in the context of a breach of state aid rules. Thus the emphasis is on the differential treatment received by Apple arising from two tax rulings from the Irish authorities and not on the tax rate of 12.5%. Nevertheless, there is some belief that this current decision emanating from the Competition DG is reflective of extreme dissatisfaction with Ireland's investment strategy in this regard.

When Ireland becomes the focus of criticism for its treatment of corporate taxation questions it is not always clear whether the criticism focuses on the low rate of corporate tax or on the tolerance of activities of which the tax ruling regarding Apple is perceived as a particularly egregious example. During the Obama administration there were some indications that Ireland was considered to be a tax haven by the US but successive Irish governments have been most anxious to ensure that this is not the reputation Ireland portrays on the global stage. For that reason Ireland has been a proactive member of the OECD BEPS project mentioned above and has also engaged pro-actively with the EU regarding other taxation matters.

> "Ireland does not meet any of the OECD criteria for being a tax haven but because of its 12.5 per cent corporation tax rate and the open nature of the Irish economy, Ireland has on a few occasions been labelled a tax haven. "[11]

FDI asset position for Ireland at the end of 2015 was a surplus of €20bn, down €148bn from the net position at the end of 2014." http://www.cso.ie/en/releasesandpublications/er/fdi/foreigndirectinvestmentannual2015/
See further www.esri.ie Report 2016 HERE

[10] Empirical research conducted in 2016 by this author relating to the presence of women on corporate boards, researched the top 100 companies in Ireland, many of whom were subsidiaries of large multinationals. This research conducted in the Companies Registration Office in Ireland www.cro.ie indicated that very large multinational companies ranging from Apple Inc. to Microsoft, Google and others have subsidiaries based in Ireland. In many cases there were a number of registered subsidiaries. On further empirical research, these subsidiaries usually take the format of being registered as private limited companies. Typically board membership includes a very small number of individuals (between 1- 5) including Irish individuals (some of whom could include a lawyer from an advisory firm, trust nominee) and 1-2 other directors resident in the US or other relevant jurisdiction).

[11] Tobin G. and Walsh, K: *What Makes a Country a Tax Haven? An Assessment of International Standards Shows Why Ireland Is Not a Tax* Haven 2013 44 Economic and Social Review (2013) This paper explores the issue of tax havens and tax competition and summarises the important work of the OECD, the EU and the G-20 in this area. The paper notes three primary reasons for the misidentification of Ireland as a tax haven in previous commentary which includes the following: "a failure to distinguish between legitimate and abusive transfer pricing; a

In stark contrast to this considered approach some commentators on Irish affairs has been critical of Ireland's position regarding its membership of the EU and the location of multinational companies. Some of this criticism has been unduly harsh. For example, Dillon argues that "that Ireland has placed itself in a false and unsustainable position in relation to the EU and the United States… Political elites in Ireland appear to hope that tax avoidance vehicles aimed at global corporations… can continue to provide jobs from multinationals headquartered in Ireland and that, even assuming the levels of prosperity seen in the boom years will not return, crisis can be avoided. Further, there is no evidence that any more complex, culturally appropriate economic planning is taking place on the part of the Irish government.[12]

By way of comparison the following tax rates pertain in some of the major economies:- [13]

Australia – 30%

Canada – 26 ½%

France – 33.33%

Germany – 30%

Netherlands – 25%

UK – 20%

Interestingly the EU as a whole comes in with an average tax rate of 20.5% compared with a global average tax rate of 24%

The Irish Government has decided to appeal the Commission's decision. Its focus is rightly on "the integrity of our tax system". [14]A second issue mentioned is whether the decision

---

misunderstanding of the role and regulation of IFSC; and a dated but influential academic paper from 1994 that incorrectly included Ireland in a list of tax havens, based on a reason that has long since lost any validity."

[12] Dillon S. Anglo-Saxon/Celtic/Global: The Tax-Driven Tale of Ireland in the European Union LEGAL STUDIES RESEARCH PAPER SERIES RESEARCH PAPER 10-63 November 18, 2010 N.C. J. INT'L L. & COM. REG. [Vol. XXXVI p. 8. This author describes this as 'the leprechaun effect' meaning that not everyone is enticed by a particular version of Irish society and culture but instead engages in an exaggerated perception of a lack of professionalism and governance, somewhat like a malevolent gnome or leprechaun. However, this more negative take on Ireland is as mythical as the positive image of Ireland based on an equally false set of premises created around the charming good leprechaun.

[13] KPMG Global Tax Rate Survey 2015

[14]The Irish Government has issued a statement through its Department of Finance, regarding its appeal of the decision of the European Commission. www.finance.gov.ie The main arguments which are summarised in STATEMENT are as follows:

"The ordinary tax rules applicable to branches in Ireland of non-resident companies are in Section 25 of the Taxes Consolidation Act 1997. The Opinions simply applied Section 25, which in accordance with the territoriality principle, taxes only the profits attributable to the branch, not the non-Irish profits of the company."

"The Commission's assertion that ASI and AOE were granted an "advantage" is incorrect. The Opinions did not depart from "normal" taxation, because ASI and AOE did not pay any less tax than was properly due under Section 25. The Commission also wrongly claims that the Opinions were selective."

concerning state aid encroaches on state competence regarding taxation, but this competency was acknowledged by the Commission. Where legitimate decisions were made by the Revenue authorities these should be defended.

Even if Ireland had decided not to appeal, it is unlikely that 13bn Euro would be repatriated to Ireland. It will be claimed by different states. Hence the US stance regarding the Commission's decision.

Finally, public discourse in Ireland is often dominated by the connection between the FDI strategy as a whole and job creation. [15] This in turn was used as a justification for appealing the EU Commission's decision. But the crux of the Commission's position is that Apple was treated preferentially, and so this is not a story about multinationals or Foreign Direct Investment in Ireland generally. Similarly, key issues raised in the appeal of the Irish government is about the integrity of the Irish tax regime. In the meantime Apple's continued investment in Ireland will serve to underline a genuine connection with the jurisdiction, both for tax purposes and in relation to access to European markets. As Tony O'Reilly once said 'It's not because the pubs are great, the golf is great and the climate is well….The fact is, it's tax.[16]

The United States.

"The Commission has exceeded its powers and interfered with national tax sovereignty"
Further arguments rely on a claim that the Commission has misapplied the 'arms length principle', the rules on state aid cannot address problems with global taxation practises such as 'mis-match' issues and the economic reality principle.
This interesting statement is also available from the website of the Fine Gael, the main government party at present (2011-present). www.finegael.ie
(Accessed May, 2017).
"1. It is simply untrue that Ireland provided favourable treatment to Apple.

The Chairman of the Revenue Commissioners has stated emphatically that:

There was no departure from the applicable Irish tax law by Revenue;
There was no preference shown in applying that law; and
The full tax due was paid in accordance with the law.
2. The Commission is undermining the fundamental principle of international tax: that tax should be paid where the value is created.

3. In the Decision, the Commission are attempting to re-write Irish Corporation Tax legislation. Taxation is a core Member State competence, which is enshrined in the EU Treaties."

[15] It would seem that the actual figure of those employed by FDI companies is about 190k compared with an overall employment figure of 1.6 million employees excluding 350k public sector employees. The numbers employed in Ireland by Apple Inc. is 5.5k. See further 'Factcheck: How many people actually work for foreign companies in Ireland. ' www.thejournal.ie September 1st, 2016. HERE

[16] Formerly Sir Anthony O'Reilly was a leading figure in Irish and US business circles holding positions over time of CEO of H. J. Heinz Corporation, former major shareholder in Irish News and Media and shareholder in Waterford Crystal *inter alia*, recently declared bankrupt in the Bahamas. . "O'Reilly told the Financial Times that Ireland's economic miracle can be attributed to the corporate tax rate of 12.5 per cent [sic]." This Week They Said, THE IRISH TIMES June 17th, 2006,

In June 2014, at an Enterprise Ireland event in San Francisco, Governor Jerry Brown of California made a jovially delivered, but pointed statement, about Ireland Inc.'s relationship to Apple. "I don't know how you got to have Apple to have so much of their business in Ireland, we thought they were a Californian company, when you look at their tax returns they're really an Irish company..." Coincidentally the European Commission launched its investigation in the same month. Some view this entire debacle as being ultimately a US problem. At the time of the unfolding of these events, the US corporation tax rate was and still is effectively 40% including a figure of 35% as a Federal tax rate plus an approximate figure of 7.5% State/local – latter can be offset against the former. As it stands this is among the worlds' highest-the global average for corporate taxation rates is 24%. Interestingly, in April 2017 the Trump Administration has promised to introduce an effective tax rate of 15%. As Tim Cook said of the monies belonging to Apple which are at issue and which currently reside in the imaginary and stateless "head office" these funds may be repatriated to the United States at some point in the future and he went on to state that Apple has "provisioned several billion dollars for the US for payment as soon as we repatriate…" He indicated at that time (September 2016) that these profits would be repatriated next year, namely 2017. Perhaps he might have been aware of the proposed reduction of the US tax rate. At this point in time some commentators are indicating that this proposed reduction may in fact be implemented as a temporary amnesty rather than a long term reduction in corporate tax.

Whether Apple Inc. owes taxes, to states within the EU or to the US is a matter for Apple Inc. Apple Inc. has indicated that it too will appeal the Commission's ruling. Apple's complaint seems to be that the rules of the game have changed and 'the goals count differently than you thought they did'.[17] Goals scored by Apple in relation to their tax liabilities, presumably.

The Commission

The European Commission began its investigation into the issue of how Apple was taxed in June 2014, and following this investigation the Commission concluded that that two specific tax rulings given by Ireland to Apple "substantially and artificially lowered the tax paid by Apple in Ireland since 1991". The rulings focussed on two Apple subsidiaries based in Ireland - Apple Sales International Ltd. and Apple Operations Europe Ltd. The Commission has asserted that these two rulings did not reflect the reality of Apple's trading operations: almost all sales profits recorded by the two companies were internally attributed to a "head office" which according to the Commission existed only on paper and could not have generated such profits. These profits allocated to the "head offices" were not subject to tax in any country under specific provisions of the Irish tax law, which are no longer in force. As a result of the allocation method endorsed in the tax rulings, Apple only paid an effective corporate tax rate that declined from 1% in 2003 to 0.005% in 2014 on the profits of Apple Sales International.

From the perspective of the Irish tax authorities however, it is incorrect to assume that Ireland would have the authority to tax an enormous level of profits which would otherwise have been attributed to the Irish subsidiary, because the Irish subsidiary would not have generated these profits from activity in Ireland. This tax ruling is incorrectly described by other commentators in terms of their understanding of Irish corporate and tax law. [18] These authors claim that the issue arose because of a difference between

[17] *Infra* n.
[18] Avi-Yonah, R; Mazzoni, G: Apple State Aid Ruling: A Wrong Way to Enforce the

how the US and Ireland treat corporate residency for the purposes of taxation. This is not the case, Ireland and States in the United States such as Delaware and California operate on the same basis in terms of determining residency, namely the place of incorporation. Ireland is not one of the European countries which focuses on central management or administration-what European's call the real seat theory.[19] Therefore the Irish tax authorities considered the Apple subsidiaries resident in Ireland as Irish companies. However, unlike the United States, Irish taxation principles do not allow for taxation of global income (the same applies to personal income). Apple had transferred its IP rights to the Irish companies. As the Commission stated "…under this agreement, Apple Sales International and Apple Operations Europe make yearly payments to Apple in the US to fund research and development efforts conducted on behalf of the Irish companies in the US." (Interestingly the idea that Apple companies in the US were conducting research on behalf of these Irish companies led Gerry Brown to state that Apple was in fact an Irish company as described above).

Because of this agreement, Apple Inc. therefore maintained that profits generated in Europe and attributable to IP rights were attributable to the Irish companies to begin with. It was this decision that was problematic for the Irish tax authorities. As the Commission observes it too has little control over this decision:- "This structure is however outside the remit of EU state aid control. If other countries were to require Apple to pay more tax on profits of the two companies over the same period under their national taxation rules, this would reduce the amount to be recovered by Ireland." Apple Sales International is responsible for buying Apple products from equipment manufacturers around the world and selling these products in Europe (as well as in the Middle East, Africa and India). Apple set up their sales operations in Europe in such a way that customers were contractually buying products from Apple Sales International in Ireland rather than from the shops that physically sold the products to customers. In this way Apple recorded all sales, and the profits stemming from these sales, directly in Ireland.

However, the next part is the really problematic issue. Apple Inc. then decided that a large part of these profits were apportioned to a 'head office' company located off shore. In light of the economic reality of

---

Benefits Principle? University of Michigan School of Law LAW AND ECONOMICS RESEARCH PAPER SERIES PAPER NO. 16-024 OCTOBER 2016 The authors state incorrectly that "Ireland adopts a central management and control test to define corporate residency for tax purposes, while the U.S. applies the place of incorporation test". (Text at fin 24). They go on "Therefore, for U.S. tax purposes, AOI, AOE and ASI were treated as Irish companies because they were incorporated in Ireland, so they were not taxed by the U.S. But for Irish tax purposes, they were treated as American companies because their central management and control were based in California." This is completely underestimating the complexity of the matter, the Irish tax authorities could not accept that they had jurisdiction to tax all of the income attributable to the Irish companies and it is in fact the income that is stateless rather than the companies.

Tobin, G. and Walsh, K*:* What Makes a Country a Tax Haven? An Assessment of International Standards Shows Why Ireland Is Not a Tax Haven 44 Economic and Social Review (2013). This paper explores the issue of tax havens and tax competition. The recent intensified debate on tax havens is summarised, as is the important work of the OECD, the EU and the G-20 in this area and the ongoing research on the economic effects of tax havens. Ireland does not meet any of the OECD criteria for being a tax haven but because of its 12.5 per cent corporation tax rate and the open nature of the Irish economy, Ireland has on a few occasions been labelled a tax haven. There are three primary reasons for this identified, each addressed in the paper: a failure to distinguish between legitimate and abusive transfer pricing; a misunderstanding of the role and regulation of IFSC; and a dated but influential academic paper from 1994 that incorrectly included Ireland in a list of tax havens, based on a reason that has long since lost any validity.

[19] *Centros Ltd v Erhvervs- og Selskabsstyrelsen* C-212/97. *Überseering BV v Nordic Construction Company Baumanagement GmbH* C-208/00

the level of activity engaged with by Apple Inc. in Ireland, the Irish tax authorities agreed that quite a lot of these profits were attributable to “head office”. This real issue for the Commission is what it considers to be the selective tax treatment of Apple in Ireland, namely the two tax rulings issued by Ireland concerned the internal allocation of these profits within Apple Sales International (rather than the wider set-up of Apple's sales operations in Europe). “Under the agreed method, most profits were internally allocated away from Ireland to a "head office" within Apple Sales International. This "head office" was not based in any country and did not have any employees or own premises. Its activities consisted solely of occasional board meetings. Only a fraction of the profits of Apple Sales International were allocated to its Irish branch and subject to tax in Ireland. The remaining vast majority of profits were allocated to the "head office", where they remained untaxed. Therefore, only a small percentage of Apple Sales International's profits were taxed in Ireland, and the rest was taxed nowhere. In 2011, for example (according to figures released at US Senate public hearings), Apple Sales International recorded profits of US$ 22 billion (c.a. €16 billion[1]) but under the terms of the tax ruling only around €50 million were considered taxable in Ireland, leaving €15.95 billion of profits untaxed. As a result, Apple Sales International paid less than €10 million of corporate tax in Ireland in 2011 – an effective tax rate of about 0.05% on its overall annual profits. In subsequent years, Apple Sales International's recorded profits continued to increase but the profits.”

Echoing the OECD and EU concern with arrangements that reflect the economic reality, the Commission went on to state that its investigation led to a conclusion that Ireland endorsed “an artificial internal allocation of profits within Apple Sales International and Apple Operations Europe, which has no factual or economic justification.”

However, the alternative approach which seems to be supported by the Commission, namely that all of the European sales should be attributed to Ireland, seems equally incorrect in terms of the economic reality. The repatriation of the profits to the US seems to be the obviously if not the entirely likely outcome if one were to consider the economic and ethical realities of the group’s activities.

Apple Inc. The Corporation and Its Culture

As stated earlier on in this piece despite the fact that there has been considerable attention paid to the role of the Commission, the decisions made by the Irish tax authorities and more recently the position of the United States, the behaviour of the corporation at the centre of this debacle has escaped with very little scrutiny. Apple Inc.’s products continue to fly off the shelves and dominate the imaginations of many consumers in the western world and beyond. However, as described a rare interview was given to the Irish national radio when this story first broke by Tim Cook CEO of Apple Inc. In my view this interview is one of the most fascinating depictions of a particular type of corporate culture. In a tone that could only be described as messianic Tim Cook first described to the RTE interviewer the complexity of the tax codes which he claimed to be so complex that a paper version would reach from the floor and up through the ceiling. What he omitted to mention of course was that the complexity of these tax codes provides opportunity for large multinational companies like Apple Inc. He constantly reiterated the relationship Apple Inc has to Ireland (and to Cork specifically)- “a joyous romance” which has been conducted since 1980. He never mentioned the figure of 13 bn but constantly reiterated how Apple Inc. was in Ireland and Cork for the long term, “like a marriage which has already lasted 37 years” and describes his visits to Ireland as being experienced as a “shot of joy”!!! He described the Commission’s ruling as unfair and wrong, in fact he described the ruling

as “maddening” and “disappointing”. He said that the ruling has no basis in fact or in law and also stated that “When you are accused of doing something that is so foreign to your values, it brings out an outrage in you.”

If the avoidance of tax to the tune of 13bn Euros is so foreign to the values of Apple Inc. how has this happened? “Apple has always been about doing the right thing, not the easy thing.”[20] You can listen HERE

Conclusion

Returning to the central hypothesis of this paper namely that the complexity of the regulatory ecology (or alternatively the theory that multi level regulation) in which corporations as big as Apple Inc. operate presents enormous opportunities for the blurring of the distinction between legality and illegality. My own view is that this gap ought to be crossed by a strong appreciation of the role of the ethical corporation. While I place the corporation’s action at the centre of these issues in terms of accountability, and argue for the development of ways which will encourage and motivate ethical and sustainable actions, I argue that sovereign states, Ireland and the federal United States in this context display legitimate expectations and interests. In particular Irish authorities faced with the ramifications of the structure of Apple’s business were left with little choice not to tax the huge amount of profit nominally repatriated to the Irish registered companies and then on to “head office”. This is about the apportionment of profits. The role of the United States, its relationship to the state of California and the relationship of Apple Inc to both must also be closely scrutinised with a view to examining options for a resolution of this matter.

[20] Milton Friedman – ‘The Social Responsibility of Business Is to Increase Its Profits’ (New York Times Magazine, 1970)